

**MidAmerican Energy Company's Initial Comments to the
Illinois Commerce Commission:**

**Federal Energy Regulatory Commission
Standard Market Design
Notice of Proposed Rulemaking,
Docket No. RM01-12**

MidAmerican appreciates the Illinois Commerce Commission's interest in the Federal Energy Regulatory Commission's Standard Market Design initiative. MidAmerican offers these comments based on its ongoing review of the Standard Market Design NOPR. MidAmerican expects to develop new comments, and to modify its current comments as necessary, as this review continues.

Overview – The proposed Standard Market Design represents a step toward better, more competitive markets

MidAmerican believes the Standard Market Design NOPR represents a positive step toward more competitive wholesale markets. We agree the current regulatory system creates the potential for discrimination. The NOPR's proposed Network Access Transmission Service, independent transmission system operation, and Standard Market Design would limit this potential.

Given the relatively slow development of RTOs in response to FERC Order 2000, MidAmerican believes FERC must take a stronger role in developing competitive markets, working toward seamless transmission borders, and encouraging new infrastructure to economically eliminate bottlenecks. The Standard Market Design NOPR has the potential to accomplish this.

MidAmerican has sought to encourage regional planning, adequate infrastructure, and broader competitive markets through its involvement in MAPP, TRANSLink, and the Midwest ISO. We believe the Standard Market Design initiative is broadly consistent

with this direction. The NOPR incorporates a number of market elements already planned for implementation in the Midwest ISO. MidAmerican anticipates that its involvement in TRANSLink and the Midwest ISO will meet FERC's standard for operation of the transmission system by an independent entity.

MidAmerican outlines specific concerns in later paragraphs of this document and believes that attention to detail is vital in effectively implementing the NOPR. However, these concerns do not diminish our overall belief that the NOPR will improve the functioning of markets.

Independent Transmission / Network Access Service

MidAmerican endorses the NOPR's concept for independent operation of the transmission system. Independent transmission operation must be an integral part of any Standard Market Design to assure a workable wholesale market.

However, MidAmerican is concerned about the introduction of yet another entity into the restructuring process. In 1992, FERC introduced Regional Transmission Groups (RTGs). In 1996, FERC endorsed Independent System Operators (ISOs) in Order 888. 1999 saw the introduction of Regional Transmission Organizations (RTOs) under Order 2000. The current NOPR would mandate system and market operation under Independent Transmission Providers (ITPs). While MidAmerican supports the concept of an independent market operator, we do not believe that the market operator must necessarily encompass all the responsibilities that the NOPR would assign to an ITP.

In addition, the NOPR seems vague as to who would qualify as an ITP. Many utilities are forming Independent Transmission Companies (ITCs), and the NOPR does not delineate clearly the responsibilities of the market operator, the independent

transmission provider function, and the independent transmission company. This adds uncertainty to the movement toward restructuring.

Transmission Pricing

Rather than setting forth a definitive pricing model, the NOPR seeks comment on a number of transmission pricing issues. In some aspects, the treatment of transmission pricing resembles a Notice of Inquiry rather than a Notice of Proposed Rulemaking.

As it relates to the embedded costs of existing transmission, it is not clear that the NOPR transitions to a defined end-state beyond the license plate model. MidAmerican finds the license plate model unacceptable due to the cross subsidies which result from its failure to align revenues with cost causation. Rather, MidAmerican supports a combination highway / zonal rate structure consistent with the TRANSLink model.

As it relates to pricing of new transmission, MidAmerican is concerned with the NOPR's apparent preference for participant funding. MidAmerican instead prefers that new transmission be provided by independent transmission companies, who in turn could use participant funding among other funding options.

The NOPR likewise does not resolve the pricing of inter-regional transactions, a significant issue in Illinois given that utilities have chosen differing RTOs. To ensure continued development of a robust, competitive wholesale market, it is vital that seams issues between ITPs be minimized. Any boundary between ITPs carries the potential to impede economic transactions, disrupt market liquidity, and affect operational reliability. FERC's July 31, 2002 order in Docket No. EL02-65-000 et. al. recognized the importance of establishing a joint and common market spanning both the Midwest ISO

and PJM. It is vital that the ultimate Standard Market Design continue to emphasize the mitigation of seams issues.

Congestion Management / Energy Markets

The NOPR proposes to manage transmission congestion with locational marginal pricing. MidAmerican believes this market-based system is superior to the current method of managing transmission congestion through administrative procedures and pro rata reductions in transactions. It is generally consistent with the congestion management scheme currently under development within the Midwest ISO.

MidAmerican supports the NOPR's proposed day-ahead and real-time markets for energy, transmission, and ancillary services. Creating these markets will foster increased price transparency, more innovative financial instruments, and overall market efficiency.

The NOPR proposes a system of Congestion Revenue Rights (CRRs) as a hedge against congestion revenue charges. Holders of CRRs would pay any transmission congestion charges in the same manner as all other transmission customers, but they would also receive back a portion of these congestion charges collected by the ITP. MidAmerican endorses CRRs as a financial tool to mitigate congestion charges, but CRRs are no substitute for eliminating congestion in the first place. Congestion resulting from an insufficient transmission infrastructure may frustrate effective market operation. It can take years to develop this infrastructure to achieve market effectiveness. Rather than relying primarily on congestion management hedging tools, MidAmerican endorses a robust regional transmission network capable of supporting a vibrant wholesale market.

MidAmerican supports the NOPR's regional approach to transmission planning, including multi-state regulatory participation. Again, such planning can only be effective in the presence of a homogeneous market which is not bifurcated by market seams.

MidAmerican does not believe holders of CRRs should have physical priority on the system when load must be curtailed. Rather, physical priority should be given to transactions identified in a customer's resource adequacy requirement.

The allocation of CRRs poses special challenges in states having retail access. The NOPR asks whether CRRs should "follow the load" as retail customers shift from one supplier to another. MidAmerican believes it is extremely important for CRRs to "follow the load" as proposed in the NOPR. This will help encourage retail access and mitigate the desire of former suppliers to "hoard" CRRs. However, MidAmerican acknowledges that a number of details are not addressed in the NOPR and must be worked out prior to implementation. For example, the NOPR does not address how former suppliers might be compensated when their CRRs shift to new suppliers under customer choice.

Regional Transmission Planning

MidAmerican supports the NOPR's call for a system of regional transmission planning. MidAmerican has long been involved with regional transmission planning through its involvement in MAPP. MAPP formed a Regional Transmission Group (RTG) with a regional collaborative planning process over a decade ago. MidAmerican's involvement with TRANSLink and the Midwest ISO should make this regional planning process even more robust.

The NOPR intends that expansion be accomplished with the most economic mix of transmission additions, generation additions, and demand response. While MidAmerican agrees that expansion should be done via the most economic means available, we object to any requirement that ITPs enter into an elaborate bidding process that may be unnecessary in many cases. While the NOPR's proposed bidding process may be of value in certain instances, (for example, in resolving regional transmission constraints), it will be of little value and will delay transmission improvements for most situations, (for example, in adding local area transmission improvements to serve new load). Therefore, the NOPR's proposed bidding process should not be mandated as a prerequisite to transmission construction.

Reciprocity

The NOPR also discusses reciprocity provisions. While the NOPR proposes to “continue the approach to reciprocity” developed in Order No. 888, there is uncertainty over how FERC will apply this. In Order No. 888, FERC determined that a customer could not receive service under an Open Access Transmission Tariff without offering service comparable to an OATT. There is uncertainty whether the NOPR's proposal to “continue the approach to reciprocity” means that

- a customer could only receive service under a Standard Market Design tariff if it also offers service comparable to a Standard Market Design tariff, or
- a customer can receive service under a Standard Market Design tariff merely by offering service comparable to an Order No. 888 OATT.

MidAmerican believes that a customer should only receive service under a Standard Market Design tariff if it also offers service comparable to a Standard Market Design tariff. Reciprocity, by its very definition, implies that before a service can be

received, a similar service must be offered. Service under an OATT is not at all similar to service under a Standard Market Design tariff. If it were, FERC would have little reason to promulgate the current NOPR.

Market Power Mitigation

If the idea of competitive electricity markets is to be readily accepted by the public, it is essential that these markets are perceived to behave reasonably. Market power monitoring and mitigation are critical to that perception, particularly while the market is still immature. MidAmerican believes the NOPR's approach to these concerns, including the creation of a market power monitor, seems reasonable. However, MidAmerican believes that adequate resource planning should eliminate the need for bid caps.

Resource Adequacy

The NOPR also calls for a resource adequacy process to ensure that adequate resources are available to serve customers. MidAmerican agrees that infrastructure must be supported through a planning process that provides for resource adequacy through a cost effective and equitable process. MidAmerican agrees with the NOPR that "spot market prices alone may not signal the need to begin development of new resources in time to avert a shortage," and commends FERC for the development of a regional resource adequacy process.

With regard to planning reserves, MidAmerican endorses the following principles:

- Planning reserves should be the responsibility of load serving entities.
- The amount of adequate planning reserves varies from region to region (where planning reserves are shared by utilities on a regional basis) and

varies from utility to utility (where planning reserves are not shared by utilities).

- Verifiable and enforceable demand response programs should qualify as planning reserves.
- The adequacy of planning reserves should be measured by a loss of load probability (LOLP) study.
- All regions should establish meaningful and enforceable mechanisms that permit reserve sharing to meet planning reserve requirements.
- Planning reserve requirements should provide for independent verification of resources and compliance.
- A long-term planning horizon should be used for evaluating compliance with planning reserve requirements.

The NOPR fails to distinguish planning reserves and operating reserves.

MidAmerican believes planning and operating reserves are separate issues to be addressed in market design.

Retail access adds an additional layer of complexity to resource planning and load forecasting. While it is possible to develop a reasonable forecast of total load within an ITP, it is difficult to develop a forecast for each load serving entity within an ITP when customers have the ability to rapidly change suppliers under retail access. It would be helpful if the adequacy requirement, like CRRs, could somehow “follow the load” if a customer switched suppliers. In general, the relationship between resource planning and retail access requires a great deal of thought given the ability of customers to move from one load serving entity to another on relatively short notice.

MidAmerican commends the NOPR for exploring demand response as a means for satisfying requirements, meeting reliability margins and controlling costs.

MidAmerican strongly recommends that demand responses be routed through individual load serving entities to ensure coordination of balancing load and resources.

The NOPR proposes to make the planning horizon a matter for regional choice, and MidAmerican concurs. The Regional State Advisory Committees should play a role in developing an acceptable planning horizon.

Implementation

While MidAmerican supports the NOPR's goals, we are nonetheless concerned with the speed at which the NOPR proposes to proceed. Several hurdles must be crossed prior to successfully implementing the goals of the NOPR:

- Accuracy of system models is vital. The NOPR will impose significant requirements for hourly load forecasting price bids, and locational marginal pricing determination at each system node.
- Successful expansion of current models is vital. Expanding the PJM model to accommodate a combined SPP-MISO-PJM system will significantly increase the amount of generating capacity and number of nodes which must be modeled.
- Development of support systems for billing, etc., is vital. Market participants must have complete confidence in the capability of administrative support systems to deliver accurate results.

While MidAmerican supports the NOPR's current timeline, it is important the market support mechanisms be fully tested and operational prior to implementing the anticipated market services.

FERC should be open to a phased approach which would implement the most important aspects of a competitive market as soon as possible while delaying less vital elements. It is not MidAmerican's goal that the overall market design be delayed; rather, a phased implementation should be used only to the extent that complete implementation cannot be accomplished on the NOPR's intended schedule.